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No. 95-372

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1995

NORMAN W. SWANSON, *ET AL.*,
Class A Petitioners, and

CHARLES L. BERRY, *ET AL.*,
Class B Petitioners,

v.

JANICE H. FAULKNER, *et al.*,
Respondents.

Petition for A Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

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BRIEF IN OPPOSITION

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20 pp

QUESTION PRESENTED

Whether the Full Faith and Credit Act, 28 U.S.C. § 1738, required a federal district court to give preclusive effect to a state supreme court's final adjudication of the same federal constitutional claims that were pending before the district court when the state court judgment was rendered?

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BRIEF IN OPPOSITION

INTRODUCTION

This case involves federal due process claims that were being litigated simultaneously in state and federal courts. The state supreme court entered a final judgment first. The district court gave the state judgment full faith and credit and entered judgment dismissing the federal action. In affirming the district court, the Court of Appeals for the Fourth Circuit correctly concluded that a "straightforward application" of the Full Faith and Credit Act (28 U.S.C.

§ 1738) and this Court's decision in *Parsons Steel, Inc. v. First Alabama Bank*, 474 U.S. 518 (1986) was dispositive and required dismissal of petitioners' claims. *Swanson v. North Carolina*, 55 F.3d 956, 965 (4th Cir. 1995). No unique or novel questions of federal constitutional or statutory law are involved. There is no compelling reason to grant this petition, and it should be denied.

COUNTER STATEMENT OF THE CASE

After *Davis v. Michigan Department of Treasury*, 489 U.S. 803 (1989), North Carolina equalized the tax treatment of State and federal pension income and gave refunds to federal pensioners who met the requirements of the applicable state tax refund statute, N.C. GEN. STAT. § 105-267 ("§ 267").[1] To obtain a refund, § 267 requires a taxpayer to pay the disputed tax and protest its legality by demanding a refund within 30 days of payment.

More than 12,000 federal pensioners met § 267's requirements and received over nine million dollars in refunds of taxes paid on their 1988 federal pension income.[2]

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[1] Years before *Davis*, the Supreme Court of North Carolina held that § 267 was the exclusive method by which a taxpayer can challenge the constitutionality of a state tax statute and obtain a refund of taxes paid under the statute. *Coca-Cola v. Coble*, 293 N.C. 565, 238 S.E.2d 780 (1977). The state supreme court has adhered to its earlier ruling in cases spawned by *Davis*. *Bailey v. North Carolina*, 330 N.C. 227, 235, 412 S.E.2d 295, 300 (1991), *cert. denied*, 504 U.S. 911 (1992); *Swanson v. North Carolina (III)*, 335 N.C. 674, 680, 441 S.E.2d 537, 541, *cert. denied*, 509 U.S. ___, 130 L. Ed. 2d 598 (1994).

[2] By its terms, § 267 limited refunds to the 1988 tax year because claims for prior-year taxes, not having been made within "30 days after payment," were extinguished.

For those federal pensioners who failed to make timely refund demands because *Davis* was decided so near the filing deadline for the 1988 tax year, the North Carolina General Assembly enacted a special tax credit permitting them to recover over a period of three years the taxes paid on their 1988 federal pension income. N.C. GEN. STAT. § 105-151.20. Thus, all federal pensioners received either a refund or a tax credit for state taxes paid on their 1988 federal pension income.

At the time of the *Davis* decision, North Carolina also excluded from state income taxation the first $1,500 of the service pay of North Carolina National Guardsmen. No comparable benefit was conferred on federal military reservists or active duty personnel who paid North Carolina state income taxes. Following *Davis* this tax benefit was repealed.[3]

In April 1989, federal pensioners who failed to meet § 267's requirements and did not receive refunds (denominated "Class A petitioners") sued the North Carolina Department of Revenue and State tax officials ("State respondents") in the United States District Court for the Eastern District of North Carolina. Early in 1990 a second class, composed of active duty and reserve members of the federal armed forces who did not receive the tax benefit extended to members of

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[3] Although North Carolina conceded that pre-*Davis* differential taxation of state and federal pension income violated the principles set forth in *Davis*, the National Guard tax benefit did not since virtually all of the service pay for national guardsmen came from the same source as federal service pay -- the United States Treasury. *See* State respondents' brief in opposition to petition for writ of certiorari to review *Swanson III* where this issue was addressed in detail. *Swanson v. North Carolina*, No. 93-1882, Brief in Opposition, pp. 24-27.

the North Carolina National Guard (denominated "Class B petitioners"), were allowed to join the action as plaintiffs. Both classes claimed that their due process rights were violated by application of § 267 to deny their refund claims. In August 1990 the district court dismissed the petitioners' monetary claims for refunds but not the claims for purely prospective declaratory and injunctive relief.

In 1990 Class A and Class B petitioners ("petitioners") sued in state court to obtain refunds. Applying *Davis* prospectively only, the Supreme Court of North Carolina held that petitioners were not entitled to refunds. *Swanson v. North Carolina (I)*, 329 N.C. 576, 407 S.E.2d 791 (1991), *adhered to on rehearing*, *Swanson v. North Carolina (II)*, 330 N.C. 390, 410 S.E.2d 490 (1991). This Court reversed and remanded the *Swanson* decisions for reconsideration in light of *Harper v. Virginia Department of Taxation*, 509 U.S. ___, 125 L. Ed. 2d 74 (1993), in which the Court held that *Davis* must be applied retrospectively. *Swanson v. North Carolina*, 509 U.S. ___, 125 L. Ed. 2d 713 (1993).

On remand, petitioners asked the North Carolina Supreme Court to remand to the trial court for judgment in their favor, or, alternatively, to allow further briefing and argument in the state supreme court in light of the *Harper* decision and the remand order. The North Carolina Supreme Court ordered further briefing and argument rather than remanding to the trial court. While the North Carolina Supreme Court was reconsidering its earlier *Swanson* decisions, petitioners returned to the United States District Court and moved for entry of a final judgment. They unabashedly sought the federal judgment to compel the state supreme court to award refunds by virtue of the preclusive

effect they contended the federal judgment would be given in the pending remand proceeding. In response, the State respondents moved for dismissal of the federal action because there was no longer any purely declaratory or injunctive relief available to them, and, therefore, the Eleventh Amendment barred the relief they sought. *Green v. Mansour*, 474 U.S. 64 (1985); *Edelman v. Jordan*, 415 U.S. 651 (1974). Further, the State respondents asked the district court to reconsider its 1990 refusal to dismiss the action pursuant to the federal Tax Injunction Act bar.

While these motions were pending, the Supreme Court of North Carolina rendered its decision in *Swanson v. North Carolina ("Swanson III")*, 335 N.C. 674, 441 S.E.2d 537 (1994), and this Court subsequently denied a petition to review that decision. *Swanson v. North Carolina*, 509 U.S. ___, 130 L. Ed. 2d 598 (1994). In *Swanson III*, the state court held that § 267 met all federal due process requirements and had been applied properly to deny petitioners' refund claims for failure to meet its requirements. The district court then granted the State respondents' motion for summary judgment dismissing petitioners' due process claims because the Full Faith and Credit Act (28 U.S.C. § 1738) required the district court to give preclusive effect to *Swanson III*.

The United States Court of Appeals for the Fourth Circuit affirmed, *Swanson v. Faulkner*, 55 F.3d 956 (4th Cir. 1994), and two petitions for writs of certiorari ensued. The present petition was filed by Class A and Class B petitioners and focuses on whether the Full Faith and Credit Act required the district court to give preclusive effect to *Swanson III*. The second petition, to which the State respondents

have separately responded, was filed by five Class A members and focuses on their individual claims that they each met § 267's requirements but nevertheless were denied refunds. (*Homesley v. Faulkner*, No. 95-373).

REASONS WHY THE WRIT SHOULD NOT BE GRANTED

The petition should be denied because the issue it presents is controlled by an unambiguous federal statute, the Full Faith and Credit Act (28 U.S.C. § 1738), and a dispositive decision of this Court, *Parsons Steel, Inc. v. First Alabama Bank*, 474 U.S. 518 (1986). As the Court of Appeals held, a straightforward application of the federal statute and the *Parsons Steel* case required the district court to give preclusive effect to the Supreme Court of North Carolina's decision in *Swanson III* in which that court adjudicated the same federal due process claims that were pending before the district court. No novel or unique question of federal statutory or constitutional law is involved, and there is no compelling reason to grant this petition.

1. THIS CASE PRESENTS A STRAIGHTFORWARD APPLICATION OF THE FULL FAITH AND CREDIT ACT AND DOES NOT PRESENT A SIGNIFICANT OR NOVEL ISSUE REGARDING THE POWER OF FEDERAL COURTS, AS PETITIONERS SUGGEST.

The nub of petitioners' argument is that the federal district court's jurisdictional finding in 1990, that § 267 was not "plain, speedy and efficient" as applied to petitioners' claims, was a final ruling that was required to be given preclusive effect thereafter. The very district court judge

who made the 1990 finding flatly rejected the contention that this jurisdictional finding was tantamount to a ruling that petitioners' due process rights had been violated, and, further, declined to give his own finding preclusive effect both because it involved a different issue from the due process question and because he held "this court's [1990] decision was non-final." *District Court's June 27, 1994 Order*, Petition, Appendix B, p. A-16.

As the district court noted, the 1990 finding was made in the context of its deciding whether the Tax Injunction Act, 28 U.S.C. § 1341, barred federal jurisdiction to hear petitioners' claims. Petitioners chose to litigate the merits of their due process claims in state court. Since they litigated their claims to finality in state court and lost, the district court was required to give the state court judgment preclusive effect. *District Court's May 6, 1994 Order*, Petition, Appendix C, p. A-25.

The Full Faith and Credit Act requires federal courts to give the same preclusive effect to a state court judgment that it would be given in the courts of the state in which it was rendered. *Kremer v. Chemical Construction Corp.*, 456 U.S. 461, 481-82 (1982); *Allen v. McCurry*, 449 U.S. 90 (1980). Moreover, this Court has held that "[o]nce the state court has rejected a claim of *res judicata*, then the Full Faith and Credit Act becomes applicable and federal courts must turn to state law to determine the preclusive effect of the state court's decision," and, further, that "even if the state court mistakenly rejected respondent's claim of *res judicata*" the remedy for "[c]hallenges to the correctness of a state court's determination as to the conclusive effect of a federal judgment must be pursued by way of appeal through the

state-court system and certiorari from this Court." *Parsons Steel, Inc. v. First Alabama Bank*, 474 U.S. at 523-25.

As the Court of Appeals held, *Parsons Steel* is dispositive of the issue raised by petitioners. In *Parsons Steel* concurrent actions arising out of the same events were pending in state and federal courts. The defendant obtained judgment in the federal action, but the state court rejected the defenses of *res judicata* and collateral estoppel and found defendants liable. The federal court then enjoined enforcement of the state court judgment on the ground that the state court action was barred by *res judicata*.

This Court reversed, holding that where a case is litigated concurrently in state and federal courts the Full Faith and Credit Act requires a federal court to give the same preclusive effect to a state court judgment as would another court of that state and that a federal court may not employ its own rules of *res judicata* and collateral estoppel in determining the effect of state judgments. *Parsons Steel*, 474 U.S. at 523. Once the state court has finally rejected a claim of *res judicata* or collateral estoppel, federal courts must turn to state law to determine the preclusive effect of the state court's decision. *Id.* at 524. Finally, even if the state court mistakenly rejected a claim of *res judicata* or collateral estoppel, federal courts must give it preclusive effect and challenges to its correctness must be pursued by appeal through the state court system and certiorari from this Court. *Id.* at 525.

In *Swanson III*, the North Carolina Supreme Court noted the district court's 1990 ruling and declined to give it preclusive effect because it was not a final judgment, citing an earlier order by the district court to that effect. *Swanson*

III, 335 N.C. at 691-92, 441 S.E.2d at 547-48. (*Petition*, Appendix E, pp. A-63 - A-65). This analysis was in full accord with the district court's 1994 orders. Without doubt, the Full Faith and Credit Act required the district court to accept the state supreme court's decision not to give preclusive effect to the district court's 1990 jurisdictional finding. Moreover, even assuming *arguendo* that the state supreme court erred, petitioners' only recourse was to seek review from this Court by certiorari. Petitioners in fact did so, and this Court denied their petition. *Swanson v. North Carolina*, 509 U.S. ___, 130 L. Ed. 2d 598 (1994).

The North Carolina Supreme Court was the first court in either the state or federal action to reach a final decision on the merits of the dispositive due process issue. Its decision in *Swanson III* was plainly entitled to preclusive effect, and, with the controlling due process issue in the case decided, the district court correctly granted summary judgment and final judgment for the State respondents.

2. THE COURT OF APPEALS DECISION WAS A STRAIGHTFORWARD APPLICATION OF THE LAW AND DID NOT CREATE A CONFLICT WITHIN THE CIRCUITS WHICH THIS COURT IS COMPELLED TO RESOLVE.

Petitioners contend that other circuits apply preclusion law in similar circumstances differently than did the Fourth Circuit in this case. The cases they cite do not support their contention. Instead, the Fourth Circuit's decision is a straightforward application of the Full Faith and Credit Act that is indistinguishable from this Court's *Parsons Steel* decision.

Petitioners' citation to *Freeman United Coal Mining Co. v. OWCP*, 20 F.3d 289 (7th Cir. 1994) is misplaced. In *Freeman* the United States Department of Labor Review Board made an administrative decision that a coal miner was entitled to total disability benefits under the Black Lung Benefits Act (30 U.S.C. §§ 901, *et seq.*). The mining company filed a motion for the Board to reconsider its decision. While the motion was pending, the Illinois Industrial Commission, applying the Illinois Workers' Compensation Act, ruled that the miner was only partially disabled. The mining company amended its reconsideration motion to ask the federal agency to give preclusive effect to the state agency's decision.

The Court of Appeals in *Freeman* reasoned that collateral estoppel did not apply "where, as here, the effort has already been undertaken in the case before the [federal administrative law judge] and the decision rendered on the merits, the reasons for collateral estoppel are hardly served." 20 F.3d at 294. Moreover, the Court of Appeals concluded that collateral estoppel was inappropriate because the issues before the state and federal agencies and the allocation of the burden of persuasion in the two administrative proceedings were different. In contrast, the district court in petitioners' case had not reached a decision on the merits of petitioners' due process claims -- the very same claims adjudicated to finality in the first instance by the state supreme court. Thus, the *Freeman United Coal Mining Co.* case has little, if any, relevance to the issue raised in the petition.

Next, petitioners rely on a partial quote from a footnote in *Instructional Systems, Inc. v. Computer Curriculum Corp.*, 35 F.3d 813 (3rd Cir. 1994) for the proposition

that the *Parsons Steel* case does not prevent a federal court from refusing to give preclusive effect to a state court decision on a federal constitutional issue where the federal court had previously established subject matter jurisdiction. This is undoubtedly true in the context of that case. In *Instructional Systems, Inc.* a federal district court abstained, pursuant to *Railroad Commission v. Pullman*, 312 U.S. 496 (1941),[4] from ruling on a federal constitutional question until the state supreme court ruled on a dispositive issue of the application of the New Jersey Franchise Practices Act which could obviate the federal question. The federal court expressly retained jurisdiction of the federal question, and pursuant to a reservation made under *England v. Louisiana State Board of Medical Examiners*, 375 U.S. 411 (1964),[5] the parties litigated the state issue to finality. In its opinion, the New Jersey Supreme Court opined that the extraterritorial reach of the state act did not violate the Commerce Clause, and when the case returned to the federal district court, one of the parties asked the court to give preclusive effect to the

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[4] This Court held in *Pullman* that when a federal court is presented with both a federal constitutional issue and an unsettled issue of state law whose resolution might narrow or eliminate the federal constitutional question, abstention may be justified under principles of comity in order to avoid needless friction with state policies.

[5] In *England*, this Court held that a party may preserve its right to return to federal court by making an express reservation in the state court that he is exposing his federal claims there only for purposes of complying with *Government Employees Organizing Committee v. Windsor*, 353 U.S. 364 (1957), and that he intends, should the state court hold against him on the question of state law, to return to the federal district court for disposition of his federal contentions. *Government Employees Organizing Committee v. Windsor* required parties remitted to state court under *Pullman* to inform those courts what their federal claims were so that the state courts had the opportunity to construe the state statute in question in light of those federal claims.

state supreme court's finding as to the Commerce Clause issue.

In the context of the procedural background in *Instructional Systems, Inc.*, the federal district court had no difficulty in deciding not to give preclusive effect to the New Jersey Supreme Court's opinion on the federal Commerce Clause issue because this was the issue the district court had reserved and which was subject to a valid exercise of an *England* reservation in the state court proceeding. In petitioners' case, there was no *Pullman* abstention, and no *England* reservation was made when the merits of their due process claims were litigated to finality in the state courts.

Next, petitioners cite two cases dealing with the application of federal preclusion principles as between federal courts. *Cycles, Ltd. v. Navistar Financial Corp.*, 37 F.3d 1088 (5th Cir. 1994); and *American Postal Workers Union v. United States Postal Service*, 736 F.2d 317 (6th Cir. 1984). Neither case involved the Full Faith and Credit Act. As this Court held in *Parsons Steel*, once a state court has rendered a final judgment on a preclusion issue federal courts are not free to apply federal preclusion principles. Thus, the *Cycles, Ltd.* and *American Postal Workers Union v. United States Postal Service* cases are inapposite.

Finally, the cases petitioners string cite on page 13 of their petition offer little, if any, support for their contention that the Fourth Circuit's decision created a conflict in the circuits. *Howell v. Thomas*, 566 F.2d 469 (5th Cir.) (*per curiam*), *cert. denied*, 439 U.S. 826 (1978), involved denial of *habeas corpus* relief to an attorney who had been adjudged to have been in contempt of court. Before the contempt judgment could be enforced, a jury found in his favor in a

disbarment proceeding on essentially the same facts underlying the contempt judgment. The federal court declined to hold that the subsequent disbarment verdict could estop the previously adjudicated contempt action. This case has nothing in common with petitioners' case.

In *Flood v. Harrington*, 532 F.2d 1248 (9th Cir. 1976), a taxpayer sued several Internal Revenue attorneys in federal court on the frivolous allegation that they violated his constitutional rights by trying to collect a tax deficiency from him in another federal action. In October 1973, final judgment was entered dismissing the taxpayer's action, and he appealed. In November 1973, summary judgment was entered for the government on the merits of the tax deficiency case. The government asked the Court of Appeals to give *res judicata* effect to the November summary judgment in the appeal of the October 1973 dismissal. The Court of Appeals declined to do so on the ground that a subsequent summary judgment could not bar a final judgment entered earlier. This case has nothing to do with the issue raised by the petition.

Clark Equipment Co. v. United States, 912 F.2d 113 (6th Cir. 1990), *cert. denied*, 500 U.S. 941 (1991), focused on whether a taxpayer was entitled to a tax deduction concerning conversion of debentures. No Full Faith and Credit Act or preclusion issues are mentioned in the opinion, and State respondents are mystified as to why this case was cited.

Maseda v. Honda Motor Co., Ltd., 861 F.2d 1248 (11th Cir. 1988), arose in the context of a state court case that was removed to federal district court based on diversity of citizenship of the parties. The main diversity claim was

dismissed but a cross claim remained over which the district court retained jurisdiction. When a state court attempted to enter an order concerning the cross claim, the federal district court enjoined the state court from proceeding on it. The Court of Appeals distinguished *Parsons Steel* on the ground that "this case does not involve a situation where concurrent jurisdiction rested with both the state and federal court . . . . Prior to a remand, the state court had a duty not to proceed in the case and any subsequent proceedings in state court were without legal effect." *Maseda*, 861 F.2d at 1256. This case has little, if any, relevance to the issue raised by the petition.

In *Kaempher v. Brown*, 684 F. Supp. 319 (D.D.C. 1988), *summarily aff'd*, 872 F.2d 496 (D.C. Cir. 1989), a federal district court held that the Full Faith and Credit Act did not prevent the court from enjoining a District of Columbia superior court action in order to protect a prior federal judgment. Applying *Parsons Steel*, the district court stated that "[t]he issue before us then is whether the Superior Court has 'finally rejected' American's claim of *res judicata*." *Kaempher*, 684 F. Supp. at 323. To answer this inquiry the court said that the threshold question was "whether the Superior Court has in fact decided the issue of *res judicata*, and second, whether if it has its ruling is a 'final' one under District of Columbia law. If both of these requirements are met, we are bound by that determination, and can not enjoin defendants from proceeding with the Superior Court action." *Id.* The district court examined the superior court judgment, found that it did not address the *res judicata* issue at all, and declined to give it preclusive effect. In so ruling, the court "interpret[ed] *Parsons* as holding that the Full Faith and Credit Act bars a federal court from enjoining a state action

in order to protect a prior federal judgment only when a state court has *expressly* rejected the claim of *res judicata*." *Id.* (emphasis is the court's). Thus, the court in *Kaempher* straightforwardly applied both the Full Faith and Credit Act and *Parsons Steel* and did not render a decision which is in conflict with the Fourth Circuit's decision in petitioners' case.

In sum, the cases petitioners cite do not support their contention that this Court should review the Fourth Circuit's decision because it somehow conflicts with the way other circuits apply *Parsons Steel*, the Full Faith and Credit Act or principles of issue and claim preclusion. Equally unavailing is petitioners' contention that the Fourth Circuit decision will create multiplicitous litigation in state and federal courts because litigants will try to obtain "two bites at the apple." *Petition*, p. 9. When federal courts give preclusive effect to a state court's final judgment adjudicating the same claims concurrently pending in federal court, the controversy ends after the first court renders final judgment on the merits. This avoids the "second bite at the apple" of which petitioners complain. Here, it is the petitioners who seek a "second bite at the apple" because they litigated the merits of their federal due process claims to finality in state court and now want to relitigate the claims in federal court because they did not like the outcome of the state court case.

3. PETITIONERS' CONTENTION THAT THEY WERE DENIED DUE PROCESS IS A REHASH OF THE SAME ARGUMENTS THIS COURT REJECTED WHEN IT DENIED CERTIORARI TO REVIEW *SWANSON III*.

Petitioners claim they were afforded a constitutionally inadequate remedy to obtain refunds of taxes they paid on their federal pensions in violation of *Davis*, citing *McKesson v. Florida Division of Alcoholic Beverages and Tobacco*, 496 U.S. 18 (1990); *Harper v. Virginia Department of Taxation*, 509 U.S. ___, 125 L. Ed.2d 74 (1993); and *Felder v. Casey*, 487 U.S. 131 (1988). All of these arguments were rejected by the North Carolina Supreme Court in *Swanson III*. Petitioners then made the same arguments in their petition for a writ of certiorari to review *Swanson III*, which this Court rejected. *Swanson v. North Carolina*, 509 U.S. ___, 130 L. Ed. 2d 598 (1994). Once again, petitioners seek an unwarranted "second bite at the apple" to relitigate the final judgment in *Swanson III*. Their transparent effort should be rejected.

CONCLUSION

The Court of Appeals for the Fourth Circuit correctly applied the Full Faith and Credit Act and this Court's decision in *Parsons Steel, Inc. v. First Alabama Bank*. There is no compelling reason to grant the petition for writ of certiorari, and it should be denied.

Respectfully submitted,

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